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June 21, 2002

Secretary William Lyons  
California Department of Food and Agriculture  
1220 N Street  
Sacramento, CA 95814

**Re: Petition for a hearing on Class 4a**

Dear Secretary Lyons:

The purpose of this letter is to petition the Department to call a hearing to consider changes to the Class 4a milk pricing formulas. The 4a formulas establish a minimum price processors have to pay for milk used to make butter and powder.

The last hearing on this issue took place in November of 2001. At that time processors sought to raise the make allowance factor in the formula to reflect the higher utility costs they faced during late 2000 and early 2001. As a result of that hearing, the department decided to raise the make allowances for butter, and more importantly powder, and thereby reduced producer prices. While Milk Producers Council disagreed with this decision, one fact that existed in the year 2001 no longer exists. Producer milk prices for the year 2001 were relatively high relative to the cost of production, and so one could argue that producers could afford a milk price reduction to help cover the higher utility costs of the processors. This is no longer true. Milk prices during 2002 are dramatically lower than 2001 and at least at this point it looks like producer prices will remain low for some time. Meanwhile, natural gas prices have returned to more historically normal levels, and so the utility costs of powder manufacturers should be significantly lower than they were during the peak energy cost period of 2000-2001.

There was talk at the Dairy Advisory Committee meeting in May about waiting until the Cost Auditing Unit finished their full cycle of cost audits before moving for a hearing, we respectfully disagree with this scenario. As a practical matter, the Cost Auditing Unit indicated that they would not be finished until late fall with their full cycle of audits. If they then did a utility update on those audits in November and then department waited until those results were known before considering a hearing, based on our experience in 2001, November utility costs would not be known by CDFA until mid January 2003. If a hearing were called for mid-January 2003, a price change would not take place until March 1, 2003, nine months from now. That is too long. The elevated natural gas prices lasted about 6 months, the extra make allowance was granted starting January 1, 2002 so we are now in our 6<sup>th</sup> month of cost recovery for the powder plants.

We would anticipate that if the department grants this request for a hearing, the hearing will be held in the first half of September 2002. Any price change from that hearing would likely be implemented on November 1, 2002. That already would give the powder plants 10 months of extra make allowance recovery. Further delay is simply unfair to producers.

There are two other items that a class 4a hearing should consider. Department staff indicated that an update of the 1998 butter and powder yield study was going to be completed by the end of August. Any data developed by that study should also be considered at the hearing we are requesting. Also, information gleaned from the Dairy Market News reports of the United States Department of Agriculture indicate that market prices for wholesale butter are consistently running above the CME – 4.5 cents, that is currently used in the 4a formula. This item also should be considered at the hearing.

We are specifically requesting that the department call a hearing on class 4a and schedule it for the first half of September 2002.

We have attached proposed language changes for Section 300.0(D)(1)(2) of the Milk Stabilization Plan. However, that language proposal is subject to change based on updated information.

We thank you in advance for your serious consideration of this petition.

Sincerely,

Geoffrey Vanden Heuvel  
Milk Producers Council

cc: Robert "Tad" Bell, Under Secretary, CDFA  
Daniel E. Webb, Deputy Secretary, CDFA  
David K. Ikari, Chief Dairy Marketing Branch, CDFA

## Proposed Stabilization Plan Language Changes

### Section 300.0 (D)

- (1) For all milk fat, not less than the price per pound computed by the formula using the simple average of the Grade AA butter price quotations for the last significant trading action for sale, offer or bid of butter at the Chicago Mercantile exchange, less a *market* adjustment of *two cents (\$0.02)*, less a manufacturing cost allowance of ten and two-tenths (\$0.102), and the result multiplied by a yield factor of 1.2.
- (2) For all milk solids-not-fat, not less than the weighted average price per pound for all Grade A and extra grade nonfat dry milk for human consumption sold f.o.b. California manufacturing plants for the period beginning the 26<sup>th</sup> day of the previous month and concluding the 25<sup>th</sup> day of the current month, less a manufacturing cost allowance of *fourteen cents (\$0.14)*; ~~multiplied by a yield factor of ninety-nine hundredths (.99).~~